



MAY 30 2002

Washington, D.C. 20201

FROM: Acting Deputy Assistant Secretary for
Grants and Acquisition Management

TO: Executive Committee for Acquisition

SUBJECT: OMB's New Capital Asset Requirements

This is to let you know that OMB has issued an updated draft of Section 300 (including the latest version of the Exhibit 300) under OMB Circular A-11 ("Planning, Budgeting, Acquisition and Management of Capital Assets"). This Section 300 represents a significant expansion from previous versions. For example, it specifically requires the use of Earned Value (EV) - - rather than giving agencies their choice of performance monitoring approaches; broadens the definition of "major" systems; calls for more stringent standards for Return-on-Investment, cost-benefit and alternatives analyses; and promises increased OMB scrutiny via business case scoring. Please note that only minimal changes to the Section 300 draft are expected when the final version is distributed later this year.

Budgetary Timeframe: On May 20, the Department's Budget Office disseminated Section 300 to your budget offices, along with a request for OPDIVs to start preparing their Exhibit 300s in the areas of construction and Information Technology. As part of the FY 2004 Budget request to the Secretary, initial drafts of the Exhibit 300s are due to our Budget Office by June 7. Exhibit 300s will need to be updated when OPDIVs submit their draft budgets to the Department in late August. Final Exhibit 300s are expected to be integrated into the HHS budget when it is submitted to OMB in early September.

Integrated Team Approach: OGAM is working closely with the Office of Budget, Technology, and Finance to implement this major OMB policy initiative in an effective and sensible manner. In addition to the May 20 Budget e-mail on the subject, OIRM issued a May 28 e-mail to OPDIV Chief Information Officers in this area. We encourage this type of partnership to be emulated at the OPDIV level. As we pointed out in our April 25 e-mail message to you, acquisition managers are a critical part of integrated capital asset project teams - - along with program management, budget, information technology, finance, logistics, and the contractor. Through early program planning, you have the opportunity to: help formulate the work statement and work breakdown structure (WBS); craft a prudent acquisition strategy; and incorporate EV requirements in major Capital Asset solicitations and contracts. At our June 13 Executive Committee for Acquisition (ECA) meeting, we plan to discuss (among other issues), the key team role that you can play in strengthening the management of your OPDIV's capital asset projects.


ATTACHMENT 1

Contractual Authorization of EV Requirements: We've enclosed Appendix C ("Earned Value Implementation Approach") of our course text for HHS's "Early Warning Project Management System Workshop". This appendix is designed to help you contractually implement EV requirements in your major construction and information technology contracts. Also, based on our review of Exhibit 300s over the last several years, CMS, FDA and other OPDIVs have had some notable successes in applying EV to major IT contracts. We encourage you to share sample EV-related solicitation and contract language with each other to promote A-11, Section 300 implementation. In fact, feel free to disseminate this sample language at our June 13 ECA meeting!

EV Training: As promised earlier, the Department will add an EV training requirement to the HHS Acquisition Regulation (HHSAR) by the end of this fiscal year. The HHSAR rule calls for all Project Officers managing Exhibit 300 projects (e.g., major construction and information technology projects) to take our "Early Warning Project Management System Workshop" - - or an equivalent EV course. To this end, please ask your cognizant project officers to budget sufficient funds for this purpose. My May 22 memo on HHS's FY 2003 Project Officer Training Program indicates that this EV class costs \$775 per student. Please note that OGAM plans to enhance its "Early Warning Project Management System Workshop" to reflect the new A-11, Section 300 requirements. In addition, OGAM and OIRM would be glad to explore other training opportunities with you, such as potentially piggy-backing on FDA's Exhibit 300 training efforts.

Next Steps: We recommend that you contact your local Budget managers to obtain a copy of the Exhibit 300, as well as detailed information about all Exhibit 300 projects that your particular OPDIV is managing. With that in hand, please offer the cognizant Project Officers your assistance in preparing: WBSs; acquisition strategies; EV implementation approaches; and relevant aspects of the draft Exhibit 300s. We'd appreciate your coming prepared to discuss these matters at our June 13 ECA meeting.

If you have any difficulty coordinating with your budget, Information Technology, or program managers in this area, feel free to call Al Schoenberg on 202-690-6361. Al would be glad to serve as your liaison to our HQ Budget and IRM offices on this matter.


Marc R. Weisman

Enclosure

cc. Catherine Tyrell
Mike Blank

Appendix C

Earned Value Implementation Approach

The following approach provides quick and effective guidance on the steps that can be taken to implement the capital asset and EV principles addressed in the *Early Warning Project Management System (EWPMS) Workshop*. The approach covers organizational practices and contractual efforts.

Organizational practices can help your project team adopt an EV methodology. They include the following:

- ◆ Encouraging supervisors to adopt an EV approach to monitor projects effectively.
- ◆ Forming integrated project teams early in the process to plan, manage and monitor projects.
- ◆ Providing rewards or recognition to employees for a job well done.
- ◆ Initiating various strategic changes in project management, as required.

Once your project has adopted an EV methodology, you need to provide a description of your performance-based management system as required by Office of Management and Budget (OMB) Circular No. A-11. See Subpart A of Part III of the Circular's Exhibit 300B, which is reproduced in this workshop handbook's Appendix A. (Exhibit 1 of this Appendix C is a sample description that can be used to meet that requirement.)

Contractual efforts can help enhance the extent to which the contractor and the Government will use a consistent EV management system (EVMS) methodology (i.e., are "singing from the same sheet of music"). They include the following:

- ◆ Using clauses in solicitations and contracts requiring the use of an EVMS (sample provided in Exhibit 2).
- ◆ Providing EVMS-related proposal evaluation criteria (sample provided in Exhibit 3).
- ◆ Formulating EVMS-related contract incentive-fee provisions (sample provided in Exhibit 4).
- ◆ Giving the contractor the discretion to use its own EV software, a commercial package, or HHS's EWPMS computer tool to generate the required data and charts.

- ◆ Retaining the flexibility to either interpret the EV data that the contractor generates (easiest approach), or put the contractor's data into HHS's EWPMS computer template for analysis.

In addition, please note that HHS views earned value (EV) as the performance-based contracting (PBC) methodology of choice for high-dollar, well-defined service projects. You can access the Web-based PBC Desk Reference at www.knownet.hhs.gov. Essentially, EV and PBC are complementary, performance-based project management tools that help you to accomplish your program missions.

*Exhibit I. Sample earned-value description for OMB Circular No. A-11,
Exhibit 300B, Part III, Subpart A*

This project is monitored by a performance-based management system developed for HHS as an Early Warning Project Management earned-value system. It is designed to help managers

- ◆ Enter cost and schedule data to track projects,
- ◆ Identify significant project deviations that require corrective action, and
- ◆ Take corrective action early in the project, as needed.

For each project, the system calculates and graphically displays the financial deviation, work deviation, financial index percent, work index percent, and budget adjustment index. It tracks such performance information for each period as data are entered, using an Excel spreadsheet. Data may be entered manually from contractors' reports or may be downloaded directly to the spreadsheet. For ease of use, the system automatically flags each deviation that is greater than 10 percent, consistent with OMB requirements.

Exhibit 2. Sample clause language for contracts requiring the use of an EVMS

In all phases, the Contractor shall provide brief monthly technical progress reports to the Government Project Monitor clearly indicating the following: contract tasks that were to be performed in the prior month; the progress made in completing these tasks; problems encountered or remaining from prior months; the expected approach to resolve problems from the prior month; tasks for the current month; and budgeting implications or significant concerns to be addressed by the Government Project Monitor.

For each task under all phases, the Contractor shall provide monthly progress reports to the Government Project Monitor—based on actual data from (or reconcilable with) its accounting system—that include the following information:

Identification of any financial variances (i.e., the difference between actual costs and budgeted costs); identification of any schedule or work variances (i.e., the difference between completed work values and budgeted costs); depiction of any variances in the form of indices and graphs; detailed reasons for any deviations exceeding $\pm 10\%$; recommended corrective actions resulting from earned-value and other performance information; and revised estimates of cost at completion based on performance to date. If subcontractors are used, the contractor must develop and implement a system to ensure that its subcontractors comply with this requirement, and each monthly progress report must address performance at the prime and subcontractor level. (For any Contractor-caused performance variances, the Contractor shall implement corrective actions, if and when approved by the Government Project Monitor; and those corrective actions shall be at no additional cost to the Government. For Government-caused performance variances, the Contractor shall negotiate with the Contracting Officer to determine appropriate corrective actions).

In addition, the first two monthly progress reports shall contain a communication plan describing how all relevant Contractor and Government personnel will be updated on cost, schedule, and technical progress—using earned-value methodology and other project performance information. Any necessary revisions to the communication plan shall be addressed in subsequent monthly progress reports.

To implement the EVMS requirements, the Contractor will need to assess the percentage of work completed under the contract. This assessment shall be based on a determination as to whether the project has reached the threshold of 0%, 25%, 50%, 75%, or 100% of the scheduled work.

The percentage used in the determination shall not be higher than the assessment of the actual work completed. Therefore, if the assessment of actual work completed falls on or between zero and 24 percent, zero shall be used; if it falls on or between 25 and 49 percent, 25 percent shall be used; if it falls on or between 50 and 74 percent, 50 percent shall be used; if it falls on or between 75 and 99 percent, 75 percent shall be used; and if all work is completed for the scheduled tasks, 100 percent shall be used.

Exhibit 3. Sample solicitation language describing proposal evaluation criteria

EVALUATION FACTORS FOR AWARD

.....Step 1 is the evaluation of the earned-value management system plan, which is pass/fail....

MANDATORY CRITERION

<u>Weight</u>	<u>Criterion</u>
---------------	------------------

Pass/Fail	1. Earned-Value Management System
-----------	-----------------------------------

Offeror must have an earned value project management system that complies with the current "Industry Standard Guidelines for Earned Value Management Systems"; or have the capability to apply earned-value analysis methods to monitor and manage the project. Use of earned value would include the capability to assign budgets to scheduled work elements (using a work breakdown structure); to credit budget values to the project as work elements are fully and partially completed (i.e., earned value); and to track actual costs incurred for the scheduled work elements.

TECHNICAL EVALUATION CRITERIA

x% Adequacy of Management Plan

....using earned value to monitor and manage project performance (a mandatory criterion).....

Exhibit 4. Sample contract incentive-fee provision

EVMS INCENTIVE-FEE PROVISION

The maximum earned-value incentive fee rate for the contract is: (applicable rate)%.

The actual earned-value incentive-fee rate = (maximum earned-value incentive-fee rate) \times (performance factor).

Performance factor = [(Work Index Percentage/100) - (Financial Index Percentage/100 - 1)].

Work Index Percentage = [(Completed Work (CW) / Budgeted Cost (BC)) \times 100

Financial Index Percentage = [(Actual Cost (AC) / Budgeted Cost (BC)) \times 100

If the performance factor is > 1 , then set it to 1.

If the performance factor is < 0 , then set it to 0.

The actual earned-value incentive-fee = (actual earned value incentive fee) \times (Budgeted Cost for each task or subtask).

The maximum earned-value incentive fee for the contract is \$\$\$\$ (maximum fee value). Any negotiated increase in the contract amount shall result in a concomitant negotiated increase in the contract's maximum earned-value incentive fee.

The above formula for calculating earned-value incentive fees shall apply to the task level rather than the overall project level. Maximum earned value incentive fees shall be identified for each individual statement of work (SOW) task and shall be based on allocating the Contractor's total maximum earned value incentive fee across SOW tasks, in proportion to the total Budgeted Cost.

For purposes of calculating earned-value incentive fees, credit for full or partial completion of work shall be granted only when tasks (deliverables) and subtasks (milestones) are due; and shall be based on a determination as to whether the thresholds of 0%, 25%, 50%, 75%, or 100% of the scheduled work have been reached and completed.

The percentage used in the determination shall not be higher than the assessment of the actual work completed. Therefore, if the assessment of actual work completed falls on or between zero and 24 percent, zero shall be used; if it falls on or between 25 and 49 percent, 25 percent shall be used; if it falls on or between 50 and 74 percent, 50 percent shall be used; if it falls on or between 75 and 99 percent, 75 percent shall be used; and if all work is completed for the scheduled tasks, 100 percent shall be used.

While the base fee of 1% may be invoiced monthly, the Government's payment of earned-value incentive fee shall be based on the Contractor's progress in completing scheduled SOW tasks and subtasks. Invoice payments for earned-value incentive-fee shall not be made more frequently than monthly. To each invoice for earned-value incentive fee, the contractor shall attach documentation that calculates the fee in accordance with the above formula and substantiates, in narrative form, the full or partial completion of associated SOW tasks.

A bilateral contract modification shall be used to make any adjustments to baseline budgets, schedules, or work elements needed in order to take into account any Government-caused delays (or other factors beyond the Contractor's control).